



RESEARCH IP

Qualitative Fund Research

Harbour Long Short Fund

27 May 2020



The views and opinions in this document are considered valid from one year from the date published.

Research Factor Weighting

Research Process Category	Model Factor Weight	Analyst Average Score	Maximum Factor Score
Corporate & Investment Governance	15%	3.50	/ 5
Investment Philosophy & Process	20%	3.40	/ 5
People	25%	3.67	/ 5
Portfolio Construction & Implementation	15%	3.17	/ 5
Risk Management	15%	3.80	/ 5
Investment Fees	10%	3.29	/ 5
Overall Average Score		3.50	/ 5

What we look at?

The qualitative rating of a fund is a function of the Research IP Research Factor Weighting process, which incorporates the following:



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Introduction

Harbour Asset Management Limited (Harbour, the Manager) formed in December 2009 and commenced operations on January 2010. Harbour is principally owned by Jarden Ltd (Jarden), at 76.3%, and the balance being owned by Harbour employees. Harbour states it is a well-resourced New Zealand based investment manager with extensive professional investment experience managing funds, further details of the Manager's core views are available [here](#).

Harbour has a group wide [investment philosophy](#), based around consistency, processes, and people. Harbour operates a [governance framework](#) that is overseen by an experienced Board which includes three independent directors. Harbour provides full transparency and independence around the investing and management of clients' money. Research IP views corporate citizenship and governance frameworks as extremely important foundations from which a manager starts to engage with the client experiences.

Harbour manages twelve retail funds, including:

- Harbour Australasian Equity Fund
- Harbour Income Fund
- Harbour Australasian Equity Income Fund
- Harbour Australasian Equity Focus Fund
- Harbour New Zealand Equity Advanced Beta Fund
- Harbour NZ Core Fixed Interest Fund
- Harbour Corporate Bond Fund
- Harbour T. Rowe Price Global Equity Growth Fund
- Harbour Real Estate Investment Fund
- [Harbour Long Short Fund](#)
- Harbour Active Growth Fund
- Harbour Enhanced Cash Fund

The funds above are managed by a team of 13 in total, of which eight manage the equity funds. The equity team comprises four Portfolio Managers, who have analyst responsibilities and are well supported by four dedicated analysts. The operations team consists of three people, and in some cases, shares resources with majority shareholder Jarden. Individual bios on the team at Harbour can be found [here](#).

Meet the Manager



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Key Takeouts

This is General Advice only and should be read in conjunction with the Disclaimers, Disclosures and Warnings at the end of this document.

Harbour Long Short Fund – Research IP Quantitative Tear Sheet

<https://platform.research-ip.com/funds/>

Note: FREE to access via registration, updated monthly including performance.

[Factsheet](#)

[Report](#)

[PDS](#)

[Articles / Views](#)

The Fund

Objectives	Harbour Long Short Fund
Investment Objectives	The Fund is an actively managed, high conviction portfolio investing principally in 'long' and 'short' listed New Zealand and Australian equities. The focus is on delivering positive returns through the market cycle by investing in long and short-sold equity positions with no particular attention to an equity benchmark. The fund is expected to have lower volatility than equity benchmarks. Given the unique features of this Fund, it may not be appropriate for all investors.
Benchmark	S&P/NZX Bank Bills 90-Day Index plus 2% Primary Benchmark - 15% S&P NZX50 Index, 15% S&P/ASX 200 Index, 70% S&P/NZX Bank Bills 90-Day Index
Alpha Objective	To deliver positive returns through the market cycle by investing in long and short equity positions.
Management Fee	1.25% management fee (GST exclusive)
Performance Fee	Performance Fee - 15% p.a. Hurdle – S&P/NZX Bank Bills 90-Day Index plus 2% Net/Gross – performance fee calculated on net out performance High Water Mark (HWM) - Yes – perpetual HWM Frequency – calculated daily, paid annually Maximum limit - There is no maximum limit.
Estimate of Total Fund Charges	1.43% (ex GST) - 2 March 2020
Minimum Timeframe	Medium to long term investment horizon. Minimum 5 years
Portfolio Structure	Portfolio Investment Entity (PIE)
Distributions	The Fund does not intend to pay any distribution, with income generated in the fund reflected in the unit price.

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The Harbour Long Short Fund ("the Fund") is benchmark unaware. The weighting to individual securities within the Fund is not made with reference to any benchmark.

Factor	Lower Limit	Upper Limit	Reference
Tracking Error			n/a
Cash Allocation	0%	130%	70%
Single Stock Limit	-15%	15%	
Sector Limits			n/a
Number of stocks			n/a
Regional limits- Australasian Equities	-30%	+60%	30%
Unlisted Australasian Equities	0%	4%	
NZ Fixed Interest	0%	30%	0%
Currency Hedging	0%	100%	
Net Equity Exposure	-30%	60%	

This is an unleveraged (maximum 60% net exposure) long short fund that is designed to exhibit lower volatility than the market, whilst allowing Harbour to express views on the stocks the team rate most highly and short sell those they rate poorly. Due to the relatively concentrated portfolio (15-25 individual long and 10-15 short), stock positions are likely to have a significant impact on the overall return of the portfolio, especially over shorter time periods (e.g. one year).

The Portfolio Manager has absolute discretion to invest across what are relatively wide allocation limits. The Fund has size restrictions built around the market capitalisation of a company, to manage risk. The Fund can own companies in the S&P/NZX10 index or S&P/ASX100 index up to a 15% position. Companies not in these indices with a market capitalisation greater than NZ\$500m can be held up to an 8% position. Other listed companies can be held up to 2%. The methodical approach to risk management is reflective of the Manager's complete process to investing client money. The Portfolio Manager leverages the analyst team to identify conviction in companies, that might be suitable for the portfolio, both for long and short positions.

Cash is a result of reduced opportunity offered by long positions, and ensuring all shorts are fully covered by cash, rather than a conscious asset allocation decision. Hedging reflects the Manager's views around country, sector, and company specific factors. Changes in hedging are likely to be significant, that is 5-10% steps or greater, rather than small incremental changes. Currency is managed at the portfolio level rather than at an individual stock level.

The Fund's flexibility is expected to result in the return of the Fund differing significantly from that of the Manager's chosen benchmark. Accordingly, investors seeking a benchmark-like return may not be suited to the Fund.

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Funds Under Management (FUM)

FUM	Harbour Long Short Fund
Fund	\$1.9m
Strategy	\$1.9m
Sector ^	\$2,430m
Manager (Australasia)	\$4,506m
Manager (Total Global)	\$4,506m
Manager comment	^ This is Harbour's only long short strategy; however, it draws on the same research platform underpinning all Harbour's long-only Australasian equity strategies.

*at 31 March 2020

The Risks

The Manager is aware of the broad range of risks, as identified in the [Product Disclosure Statement \(PDS\)](#), and is mindful of them when constructing and managing the portfolio.

The Fund can take significant positions relative to the underlying indices, however its stock-specific risks are lower than Harbour's other Australasian equity funds. The short positions are agnostic to benchmarks, but there can be and is pairing or matching of long positions and short positions within sectors as part of Harbour's risk management approach.

Importantly Research IP highlights all shorts are fully covered by cash. This approach can inflate the cash holding of the Fund, and therefore appear that the Manager is not deploying capital. Research IP considers fully covering all short positions with cash as a mandatory requirement for long-short funds in general.

Research IP notes short selling has the ability to enhance fund performance, but also has the potential to produce uncapped losses. Therefore, manager skill is extremely important. This is also an investment strategy that is not readily replicable by a retail investor or financial adviser.

Active management of currency hedging is within a range of 0-100% of Australian dollar exposure. Currency exposure is managed in the derivative market using forwards and currency swaps.

The fund can borrow, use derivatives and short sell securities. The Fund also has the ability to own debt and convertible securities and participate in stock lending programmes. The Fund can interfund into other Harbour vehicles.

Using this Fund

The Fund is one of the very few strategies that employs shorting across Trans-Tasman equities. Importantly the Fund does not use derivatives (options) to take short positions, rather it uses stock borrowing. It is important that investors understand the methods of shorting stocks, and in particular the risks associated with shorting the Trans-Tasman equity holdings.

Research IP believes the Fund is best used as a 'satellite' strategy, as the Fund may not provide a broad diversified exposure to the Australasian share market and carries heightened potential risks.

The Fund is subject to equity market risk and movements (both positive and negative) in the share prices of the underlying securities in the portfolio. Accordingly, investors should therefore be aware that the Fund may experience periods of negative returns and that there is a risk of potential capital loss being incurred on their investment. The Fund is suited to higher risk profile investors with a minimum investment time frame of five years.

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What the Manager says?

Insight	Manager view	Research IP opinion
<p>Who is accountable for managing the fund?</p> <p>Is the investment teams work history relevant to the funds they manage?</p>	<p>Craig Stent is PM, with Oyvinn Rimer in charge of risk monitoring and assisting in the managing of the fund. Craig is Head of Equities and portfolio manager for the Harbour Equity Income Fund and Harbour Long Short Fund. Furthermore, Craig provides equity research and ratings on the utility sector. Prior to joining Harbour Asset Management, Craig was employed by AllianceBernstein New Zealand for seven years.</p> <p>Oyvinn is responsible for equity research and ratings on the agriculture, resources, food & beverages, retail, and oil & gas sectors. Oyvinn also provides macroeconomic input to the wider Harbour team on the Chinese economy, which he covers through regular research trips to China. He helps run the Harbour Long Short Fund. Prior to joining Harbour Asset Management, Oyvinn was employed by AllianceBernstein New Zealand</p>	<p>The Portfolio Manager Stent has 20 years of industry experience, although a shorter manager tenure at 10 years since the commencement of Harbour. Stent has held responsibility for the Fund since its inception.</p> <p>While Stent carries accountability for the Fund, the full equity investment team provides analyst support. Ultimately this Fund leverages the best ideas of all Harbour equity funds.</p> <p>Oyvinn Rimer, with 13 years' industry experience, including 10 years since the commencement of Harbour, facilitates a critical role of risk management. With the ability to short, the risks in this Fund are compounded. Research IP believes the additional risk oversight and assistance to Stent is a positive aspect to management of oversight of the potential to compound losses.</p> <p>The tenure of the investment team is strong, with Andrew Bascand, Craig Stent, Oyvinn Rimer, and Kevin Bennett being at the Manager since commencement.</p> <p>Since commencing investment operations in 2010, the Manager has added resources, building out the team as required. The continual team development has seen new analyst additions on a consistent basis.</p> <p>Research IP notes that the Manager has one of the larger equity investment teams, and pleasingly continues to invest in the investment teams, and importantly the business. Research IP commends the Manager for looking beyond today, and investing for the future, including that of investors.</p>
<p>Has the CIO/ PM personally invested in the Fund? Are they paying the same fees as other investors?</p>	<p>The Portfolio Manager and a number of the analysts have a meaningful portion of their personal assets invested alongside clients on a full fee-paying basis. Each year a portion of the investment staff's discretionary pay is invested into Harbour Funds with a three-year vesting period.</p>	<p>Research IP believes that the interests of investment personnel are better aligned to those of the investors, when investment personnel are significantly invested, and at the same fees.</p> <p>Research IP believes the vesting of discretionary remuneration of Harbour</p>

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		<p>staff is a strong enhancement to the alignment with investors. Naturally Harbour staff want to maximise their outcomes, without excessive risk.</p> <p>Harbour uses this fund as an allocation in its diversified strategies.</p>
Why would you allocate to this fund?	<p>The focus is on delivering positive returns through the market cycle by investing in long and short-sold equity positions with no particular attention to an equity benchmark. The fund is expected to have lower volatility than equity benchmarks. The investment objective of the Fund is to deliver positive absolute returns through the economic cycle with low volatility and low correlation of returns with equity markets.</p>	<p>The Manager outlines its case as to why Harbour should be considered by an investor. The Manager also provides a series of links that outline their set of core values. Harbour believes these factors differentiate them from peers, across their product suite. Research IP believes that in conjunction with a disciplined approach to investing, the Manager presents a clear rationale as to why a potential investor should consider investing in this Fund.</p> <p>This is a strategy which aims to deliver better returns than cash by allocating a proportion of the fund to shares, but also by selling shares short. Research IP believes the Fund is best used as a 'satellite' strategy, as the Fund will not provide a broad diversified exposure to the Australasian share market and is designed as an absolute return strategy.</p> <p>When short selling, or shorting a stock, Harbour are essentially borrowing the shares. The Manager borrows shares from an existing owner. The Manager sells the borrowed shares at the current market price. The Manager believes the share's market price will decrease before they are forced to pay back the borrowed shares, allowing the Manager to pocket the difference in the two share prices. Research IP notes this is where the greatest risk of the portfolio lies. Shorting has the potential to produce unlimited losses in the portfolio. Therefore, investors should proceed with caution.</p> <p>However, Research IP believes this is an investment strategy that is very difficult for a self directed investor or financial adviser to replicate themselves and therefore warrants consideration.</p> <p>The net equity exposure of the fund can range between -30% and +60%. Gross</p>

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		<p>equity exposure can be up to 200% of the net asset value of the Fund. At 31 March 2020 the fund held a net long position of 16%. This was made up of 41% long exposure (22 positions) and 25% short exposure (13 positions). Cash was held in the Harbour Enhanced Cash Fund, NZD, AUD and futures margin / collateral to cover the short positions.</p> <p>Research IP also notes that although this Fund will have a strong bias to equity risk, it also has the ability to own debt and convertible securities, as well as use derivatives (options and exchange traded futures).</p>
What are key factors in the buying and selling decisions of the Fund?	<p>The key factors are the analysts' ratings and views on a particular stock alongside the quantitative screen which provides information signals on the longs and shorts. A view is also taken on diversification across sectors and ensuring there is no dominant factor tilt although the portfolio will generally have a growth bias. Asset allocation committee also provides a broad discussion platform in deciding on how much net equity exposure we want to have in the portfolio versus the neutral net 30% net long.</p>	<p>Research IP observes the Manager's process is one of the more methodical, well structured, and consistently implemented. Research IP believes this is a core foundation block necessary to operate this Fund's strategy.</p> <p>The Manager's process is underpinned by fundamental, bottom-up research. The long and short positions are a direct result of this proprietary process. The Manager compliments this by its strong internal research, with some external research inputs. External sources include sell-side brokers, independent research houses, as well as other data sources, although the Manager relies heavily on in-house investment models.</p> <p>The Manager's fundamental bottom up process starts with a focused approach to quantitative filtering. This distils down to the three key factors that are company specific, rather than macro focused. It is the start of the company ranking process. Research IP believes this ranking process is critical to identifying long and short positions.</p> <p>The Manager is not a quantitative manager, as the analyst team undertakes significant and detailed qualitative reviews of all companies, which enables the Manager to understand the company and its growth prospects, prior to investing in them. Research IP believes qualitative overlays, particularly with respect to shorting, is critical. This is</p>

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		<p>where the analysts scoring a series of factors, leading to a qualitative ranking, is important.</p> <p>Both quantitative and qualitative scores become a key component of the monitoring process. A deterioration of the company score will assist in the sell decision process. Deterioration of key company scores will trigger a review, which can lead to reducing the position size or exiting the company. While this may be a sell trigger for a long only position, this can be the buy signal for a short position.</p> <p>The Fund has a relatively concentrated portfolio of long positions at 15-25 holdings and 10-15 short positions. For the long positions Stent filters the analyst team for their 2-3 best ideas, which will be considered for the Fund. Stent takes some guidance around portfolio construction from the Australasian Equity and Focus Funds, and Rimer provides the risk management frameworks around the short positions. Research IP notes this Fund can take a different view to its more diversified sibling. The Manager can hold cash if no opportunities can be identified, that is there is no padding out the number of companies in the portfolio.</p> <p>The Manager must critically evaluate each position regularly and exit companies that have not met or are unlikely to meet expected growth expectations. The evaluation process is of greater importance with respect to the short positions, as they have potentially uncapped losses if not managed appropriately.</p> <p>Selling of stocks in the portfolio is a direct result of Harbour's proprietary scoring and stock ranking system. As a company falls from green, to amber to red sections of the stock scores the size of the position is reduced until it hits the lowest scoring or red section of the stock list. This is not a mandatory signal to sell, but portfolio holdings in the red section are typically turnaround stories where the Manager believes the company and its current</p>

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		pricing will improve, and the manager has sufficient conviction to invest early.
What are the key drivers of the Fund's performance and risk measures?	<p>An active research-driven investment process which principally invests in a focused selection of companies highly-rated by Harbour investment analysts and largely consistent with the overweight positions in Harbour's core Australasian Equity Fund. As a result, the Fund invests in equities which portfolio managers have high conviction in. The Fund will hold 'long' equity positions across the NZ and Australian share markets reflecting our conviction in companies which can provide medium to long term capital growth. The Fund will also be able to 'short-sell' securities. These will typically be companies which rank poorly on fundamental and quantitative signals. The Fund will also hold cash and utilise currency management to generate returns</p>	<p>The Fund's performance reporting is available via the Research IP Quantitative Tear Sheet, on the Manager's website and the Disclose website. Highlighting the Funds' performance over time and the volatility of that performance.</p> <p>This is a portfolio of 15-25 companies on the long side plus an additional 10-15 on the short side and is designed to experience lower market volatility than long-only equity funds. The short strategy deployed by the Manager has the ability to dampens the Fund's volatility compared to market. This can lead to potentially large variance in performance compared to the Fund's hybridised market based benchmark.</p> <p>Research IP believes the Funds' performance reflects Stent's security selection and Rimer's risk management overlays and assistance with security selection. The Managers' growth style bias leverages the input of the investment team and through the internal Investment Committee.</p> <p>Research IP notes that as a growth fund manager, the long portfolio positions are typically longer term holdings at 3 years or more. The holding period of the short positions varies from a few days to a few months. Needless to say they are held for a shorter period than the long positions. Even with the shorts, the concentrated nature of the portfolio is retained and does not allow the Manager to hide, should a company perform differently than expected. Investors can expect overall portfolio turnover to be higher than other Harbour long only equity funds.</p>
On what basis are the fees charged justified?	<p>Harbour's fees are transparent. There are no buy/sell spreads or entry/exit fees. The Long Short Fund has a total fee (excluding GST) of 1.43% p.a. including investment management, Supervisor, legal and audit fees as well as the costs of unit pricing, investment accounting and custody.</p>	<p>The Funds' basic fee is above the sector peer average. The Fund is one of three Harbour funds and one of 22 out of 36 peer funds to charge a performance fee in the Alternatives Sector. Detailed explanation relating to the performance fee can be found in the Other Material Information Documents. This is available</p>

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	<p>As stated in the PDS, we may be entitled to a performance fee within the Long Short Fund, which would be paid annually, following 31 December, subject to outperforming the S&P/NZX Bank Bills 90-Day Index (the Hurdle Rate) plus 2% and the HWM. The performance fee is 15% of the Fund's return above the Hurdle Rate (plus GST).</p>	<p>on the Manager's website, and the Disclose website.</p> <p>Research IP believes that performance fees should only be charged when the base management fee is significantly below the sector peer average fee. Therefore, the total cost of this fund would be at the upper end of the peer group.</p> <p>Research IP also notes the performance fees are uncapped, although a high water mark is used.</p> <p>Research IP believes that the fee structure for this Fund is high. The base fee is high and the cash hurdle is low, while the investor is still potentially exposed to significant downside risk.</p> <p>Research IP highlights there should be a direct alignment between the manager's remuneration and the performance of the Fund relative to its benchmark. Research IP believes there is an opportunity for the Manager to revisit the current fee schedule for the Fund, particularly the hurdle rate for the calculation of performance fees.</p> <p>Although Harbour notes that they can typically cross trades and therefore do not charge a buy/sell spread, it should be noted that this is not always the case and existing unit holders may incur the cost of transactions.</p>
<p>Describe the quality of the organisational and investment governance processes?</p>	<p>At the organisational level, Harbour's Board is led by an independent chair. Two other independents ensure client's best interests are put first, including a former experienced Portfolio Manager who chairs the Audit & Risk Committee.</p> <p>We have rigorous daily compliance procedures that ensure the portfolio is invested in adherence with its guidelines.</p> <p>We engage PWC to test the firm's operational and compliance processes. This assesses tasks such as the handling of client funds, investment management processes, trade execution, segregation of duties etc.</p>	<p>The Manager has a strong governance structure which starts with the composition of the Board and leadership of key Board Committees. In addition to outsourcing some functions, there are sufficient internal operational personnel, which continues to grow. This ensures the investment team can concentrate on managing the portfolios, with appropriate oversight.</p> <p>The use of external directors for the Harbour Board is considered to be in line with industry best practice. The use of external non-executive directors is strong, this excludes those representing the major shareholder, Jarden. Research IP</p>

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	<p>This is an external and independent assessment of our processes.</p> <p>Lastly, an internal risk committee periodically scrutinises the Portfolio Manager's decision making and risk allocation.</p>	<p>notes the use of independent members extends to Board delegated committees, and investment committees.</p> <p>Harbour has a formal investment committee, which meets on a monthly basis, and is chaired by Chris Di Leva, who is Harbour's Multi Asset Specialist. Research IP believes the structured investment committee process formalises a process and provides oversight to the investment decisions.</p> <p>Research IP considers the Head of Compliance reporting directly to the Board and Audit Committee as being in line with global best practice, which is not always the case in New Zealand.</p> <p>The Manager uses Bloomberg AIMS for pre and post trade compliance. This is used across all funds.</p>
Describe the Manager's ESG, Corporate Sustainability policies and engagement.	<p>Harbour integrates ESG analysis into its security selections processes. We conduct an annual corporate behaviour survey with potential equity investments. The results of this survey directly impact the weight a company is held in the portfolio, with strong corporate citizens being held at a higher weight than poorly behaving corporates. This, along with our engagement of companies, helps to drive better outcomes.</p> <p>In fixed interest securities where the risk profile is asymmetric (either you are paid back or the company defaults) we will simply not hold a company's debt if we believe its behaviour is egregious or it participates in a sector that makes investment untenable (examples include gaming). Harbour has been recognised for its ESG approach by strong scores by independent agencies UN PRI and RIAA.</p> <p>At Harbour, sustainability has been included in our key business objectives.</p>	<p>Research IP notes that Harbour have included Responsible-Investing factors in their process since inception and is viewed positively. Notably Environmental ("E") and Social ("S") factors are treated differently to Governance ("G"). Governance is well established, the relationships between companies and the environmental and social aspects are less defined.</p> <p>The Manager's internally developed ESG process is considered to be very robust and can be applied to a company, regardless of its domicile.</p> <p>Harbour is also a signatory to the UNPRI. Investors should be aware that ESG and the United Nations Principles of Responsible Investing (UNPRI) are relatively loose and that ESG integration has a broad range of interpretations.</p>
Is there alignment with the interests of investors through ownership of the Manager and/or remuneration of the investment team?	<p>Yes. The investment team invests alongside unit unitholders by personally owning units in the fund. In addition, the performance of the fund against its objectives influences investment team short and long term remuneration. A portion of the investment team's discretionary remuneration is vested</p>	<p>By being partially owned by its employees and directors, there is strong buy-in from the team to work hard for the firm's long-term success - this is good news for investors. The Manager's continual development of and commitment to its staff is viewed as market leading.</p>

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Insight	Manager view	Research IP opinion
	<p>into Harbour funds over a period of three years. This discretionary pay is in turn determined by the Fund's performance amongst other factors such as client satisfaction. Harbour is 24% owned by its employees. A long-term incentive scheme sees annual awards of further equity ownership for staff.</p>	<p>There is alignment between the bonus component of staff remuneration and the performance of the funds/portfolios. Research IP believes that Stent and Rimer have personal investment in the Fund, largely via vested short term incentives. This is viewed as a strong alignment to investor experience.</p> <p>Research IP highlights that Harbour's vesting of short-term incentives (cash bonuses) in the Manager's suite of funds is market leading from a New Zealand perspective. This brings enhanced staff tenure and alignment to the interests of investors.</p> <p>The support of largest shareholder, Jarden, is also significant, in both financial terms and operational support.</p>

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Research IP is a specialist investment research provider which is used and trusted by investors & financial advisers for investment, KiwiSaver, Superannuation and other Pension schemes throughout the Asia Pacific region.

Research IP has grown its team and footprint by utilising the specialist skills of its analysts which include;

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- ❖ equity, bond, and alternative asset specialists
- ❖ portfolio managers
- ❖ asset allocation analysts
- ❖ and ratings specialists.

Our experience has been gained in well over 20 years of roles across different facets of the industry, so we understand the key drivers and challenges for managers, as well as the impact for investors and the Financial Advice industry.

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Research IP delivers high quality quantitative and qualitative fund research to financial advisers and the broader financial services industry. Research IP works with a number of expert providers to source this data. Quantitative data is supplied by a variety of sources, including directly from the Fund Manager, while qualitative research is provided by Research IP.

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